BEFORE THE STATE BOARD OF EQUALIZATION

OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of)
)
ALLRIGHT CAL., INC.)

Appearances:

For Appellant: Norman Rasmussen
Attorney at Law

For Respondent: Kendall E. Kinyon
Counsel

O P I N I O N

This appeal is made pursuant to section 25667 of the Revenue and Taxation Code from the action of the Franchise Tax Board on the protests of Allright Cal., Inc., **against** proposed assessments of additional franchise tax in the amounts of $7,301.95, $7,054.59 and $12,120.15 for the income years ended June 30, 1968, 1969 and 1970, respectively, and on the protests of Allright Cal., Inc., as successor in interest to Allright San Diego Parking, Inc., against proposed assessments of additional franchise tax in the amounts of $171.11 and $171.11 for the taxable years ending June 30, 1970 and 1971, respectively. For purposes of assessment and appeal, appellant Allright Cal., Inc., also represents Allright Los Angeles, Inc., Allright San Francisco, Inc., Allright San Diego Parking, Inc., Victoria Auto Parks, Inc., and Security Auto Parks, Inc.

The issue for determination is whether appellant and its affiliated corporations are engaged in a single unitary business.

Appellant is one of a large nationwide group of approximately 95 wholly owned subsidiaries of Allright Auto Parks, Inc., whose headquarters is in Houston, Texas. The principal business of almost all of the subsidiary corporations is the operation of automobile parking lots at various locations throughout the United States. No single subsidiary owns or operates parking lots or any other property in more than one state. Parking lot operations in California are conducted by six different corporations with lots in the Los Angeles, San Francisco, San Diego and Long Beach areas. Each corporation is responsible for the hiring, firing and training of its personnel, does its own purchasing, and personally owns or leases all assets used in its business activities. All leased assets are leased from unrelated third parties. Over 80 percent of the subsidiaries use the name "Allright" in their corporate title. Notwithstanding this fact, no national advertising is conducted by the parent or any of the subsidiaries. Any advertising conducted by any of the companies is purely local in nature. The subsidiaries' tax returns are prepared at the home office, apparently by Arthur Young and Company, and signed by an officer of the parent.

The parent, Allright Auto Parks, Inc., is basically a holding company, but it did provide services to its subsidiaries during the appeal years for which it received substantial payments. These services were primarily technical in nature, such as the acquisition of new locations, lease negotiations and financing. Since the parking facilities of most of the subsidiaries are leased, Robert Hodspeth, the parent's vice president in charge of real estate and leasing, reviews and approves all leases. Final site selection is also controlled by the parent. The parent also borrows money on its own credit and then loans it to the various subsidiaries to facilitate major site acquisitions. As reimbursement for the services performed during 1968, 1969 and 1970, the parent received $528,669, $590,990 and $587,637, respectively. Notwithstanding the reimbursement received from the subsidiaries, the parent sustained a net loss in each of the appeal years before consideration of the dividends received from the operating companies. The parent also has established a pension plan for itself and its subsidiaries. Each subsidiary, at its option, may elect to participate or not to participate in the group plan. For the years in issue, the California subsidiaries elected not to participate in the plan.

The parent has two subsidiaries not engaged in the parking lot business. One of these is an insurance agency which places insurance for all the other companies within the group. Premiums charged by the agency to the operating companies, including appellant, are in the identical amount that the operating companies would incur if they had contracted for their insurance coverage separately. Presumably, however, the agency receives fees or commissions from the insurance companies for placing the insurance. The other nonparking lot subsidiary operates a computer service bureau. Each of the operating companies develop their own initial accounting source data which the service bureau processes on its computer to develop the necessary financial statements used by the operating companies. The cost of these accounting services is prorated to the operating companies. The service bureau operates at a break-even level and the operating companies pay a much smaller charge than they would incur if they performed this function individually or if they contracted individually for such services with an independent third party. The service bureau received $300,000., $339,485 and $368,372 in 1968, 1969 and 1970, respectively, from the operating subsidiaries for accounting services.

The record indicates that the parent has 15 directors and six officers. The parent's chairman of the board of directors is also the president of five of the subsidiaries. None of the parent's six officers serve as officers of any of the subsidiaries, although three of them are also directors of the parent. In addition to the chairman of the board, eight of the parent's directors are also presidents of operating companies. However, the presidents of the approximately 85 remaining operating subsidiaries are neither officers nor directors of appellant. The parent's remaining three directors apparently are not associated with any subsidiary. None of the officers of the California corporations are either officers or directors of the parent.

When a taxpayer derives income from sources both within and without California, it is required to measure its California franchise tax liability by its net income derived from or attributable to sources within this state. (Rev. & Tax. Code, § 25101.) If the taxpayer is engaged in a unitary business with affiliated corporations, the amount of income attributable to California sources must be determined by applying an apportionment formula to the total income derived from the combined unitary operations of the affiliated companies. (See Edison California Stores, Inc. v. McColgan, 30 Cal. 2d 472 [183 P.2d 16] (1947); John Deere Plow Co. v. Franchise

Tax Board, 38 Cal. 2d 214 [238 P.2d 569] (1951), app. dism. 342 U.S. 939 [96 L. Ed. 1345] (1952).)

The California Supreme Court has determined that a unitary business is definitely established by the existence of: (1) unity of ownership; (2) unity of operation as evidenced by central purchasing, advertising, accounting and management divisions; and (3) unity of use in a centralized executive force and general system of operation. (Butler Bros. v. McColgan, 17 Cal. 2d 664, 678 [111 P.2d 334-j (1941), affd., 315 U.S. 501 [86 L. Ed. 9911 (1942).) The court has also held that a business is unitary when the operation of the business within California contributes to or is dependent upon the operation of the business outside the state. (Edison California Stores v. McColgan, supra, 30 Cal. 2d at 481.) These principles have been reaffirmed in more recent cases. (Superior Oil Co. v. Franchise Tax Board, 60 Cal. 2d 406 [34 Cal. Rptr. 545, 386 P.2d 33] (1963); Honolulu Oil Corp. v. Franchise Tax Board, 60 Cal. 2d 417 [34 Cal. Rptr. 552, 386 P.2d 40] (1963).)

The existence of a unitary business may be established if either the three unities or the contribution or dependency test is satisfied. (Appeal of F. W. Woolworth Co., Cal. St. Bd. of Equal., July 31, 1972.) Implicit in either test, of course, is the requirement of quantitative substantiality. (Appeal of-Beatrice Foods Co., Cal. St. Bd. of Equal., Nov. 19, 1958; Appeal of Public Finance Co., Cal. St. Bd. of Equal., Dec. 1958; see also Superior Oil Co. v. Franchise Tax Board: supra.) In other words, corporations are engaged in a unitary business within the scope of either test if, because of the unitary features, the earnings of the group are materially different from what they would have been if each corporation had operated without the benefit of its unitary connections with the other corporations.

In determining that the parent and all of its subsidiaries were conducting a single unitary business respondent relied on the following factors: common ownership; some interlocking of officers and directors; centralized overhead functions such as insurance, accounting and preparation of federal and state tax returns; the common use of the name "Allright" by more than 80 percent of the subsidiaries; the availability of a common pension plan for the parent and its subsidiaries; and the parent's furnishing of financing and services relating to site acquisition and lease negotiations. Respondent's determination that appellant is engaged in a unitary business with its parent and the parent's other subsidiaries is

presumptively correct and the burden to show that such determination is erroneous is upon appellant. (Appeal of John Deere Plow Company of Moline, Cal. St. Bd. of Equal., Dec. 13, 1961.)

Initially, appellant agreed in substantial part with the facts related above. Thereafter, appellant denied many of the factual allegations originally admitted. In this regard appellant has made contradictory statements on a number of important factual points. Despite requests to submit information in support of its contentions and to explain its contradictory positions, coupled with ample time in which to respond, appellant has offered nothing. In light of appellant's failure to clarify its contradictory positions, we are compelled to conclude that the facts related above are correct. We believe that, when viewed in the aggregate, the unitary features relied upon by respondent demonstrate a degree of mutual dependency and contribution sufficient to establish the existence of a unitary business operation by the parent and all the subsidiaries. 1/ It is true that in this appeal we do not have the overwhelming number and degree of unitary characteristics that were present in cases involving more complex operations. (See, e.g., John Deere Plow Co. v. Franchise Tax Board, supra; Superior Oil Co. v. Franchise Tax Board, supra; Honolulu Oil Corp. v. Franchise Tax Board, supra.) As appellant has stated, however, there is nothing complicated or sophisticated about the parking lot operations involved in this appeal. Accordingly, we do not expect the indicators of unity to be as extensive or as permeating as those appearing in the more complex operations noted above. It is readily apparent in this matter, however, that everything that could be centralized has been centralized.

Appellant argues that in view of the unique nature of its parking lot operations, separate accounting results in a more precise and equitable method of reporting income. This contention is based upon the premise that appellant's activities are confined to a specific geographical area, that intercompany charges are determined by an arm's-length standard, and that alleged higher

1/ In reaching this conclusion we place negligible weight on the use of the "Allright" name by many of the subsidiaries. In this instance little significance can be attached to the use of a common name in the absence of any common promotion of that name.

California labor rates and property values result in shifting income from other states to California. All of these arguments were considered and rejected by the California Supreme Court in John Deere Plow Co. v. Franchise Tax Board, supra. In John Deere the court held that even if a taxpayer maintained accurate and precise accounting records, if the business was unitary, separate accounting could not be used. The allegation of distortion resulting from higher labor and property costs was rejected by the following statement:

> . . . the formula used must give adequate weight to the essential elements responsible for the earning of income ... but its propriety in a given case does not require that the factors appropriately employed be equally productive in the taxing state as they are for the business as a whole. Varying conditions in the different states wherein the integrated parts of the whole business function must be expected to cause individual deviation from the national average of the factors in the formula equation, and yet the mutual dependency of the interrelated activities in furtherance of the entire business sustains the apportionment process. (John Deere Plow Co. v. Franchise Tax Board, supra, 38 Cal. 2d at 224-225.)

Appellant also argues that, in view of the nature of the operation of the affiliated group, California is prohibited from imposing a tax on or measured by net income by Public Law 86-272 (73 Stat. 555 (1959), 15 U.S.C. § 381). Public Law 86-272 provides a limited immunity from state taxation of income derived within the state from interstate commerce where the only business activities within the state are the solicitation of orders within the state for tangible personal property. Since appellant is engaged in the business of leasing or renting parking space and does not deal in tangible personal property, its activities are excluded from the limited immunity of Public Law 86-272 by the very terms of the statute.

Finally, appellant urges that the application of the three-factor formula discriminates against it, and consequently violates the due process and equal protection clause of the Fourteenth Amendment to the United States Constitution. It has been the longstanding policy of this board to refrain from deciding constitutional questions in an appeal involving proposed assessments of additional tax. (Appeal of Maryland Cup Corp., Cal. St.

Bd. of Equal., March 23, 1970; see also Cal. Const. art. III, § 3.5.) This policy is based upon the absence of any specific statutory authority which would allow the Franchise Tax Board to obtain judicial review of an adverse decision in a case of this type, and our belief that such review should be applicable for questions of constitutional importance. This policy properly applies to the instant case.

O R D E R

Pursuant to the views expressed in the opinion of the board on file in this proceeding, and good cause appearing therefor,

IT IS HEREBY ORDERED, ADJUDGED AND DECREED, pursuant to section 25667 of the Revenue and Taxation Code, that the action of the Franchise Tax Board on the protests of Allright Cal., Inc., against proposed assessments of additional franchise tax in the amounts of $7,301.95, $7,054.59 and $12,120.15 for the income years ended June 30, 1968, 1969 and 1970, respectively, and on the protests of Allright Cal., Inc., as successor in interest to Allright San Diego Parking, Inc., against proposed assessments of additional franchise tax in the amounts of $171.11 and $171.11 for the taxable years ending June 30, 1970 and 1971, respectively, be and the same is hereby sustained.

Done at Sacramento, California, this 9th day of January, 1979, by the State Board of Equalization.

_____, Chairman

_____, Member

_____, Member

_____, Member

_____, Member